Supreme Court, U.S.
FILED
AUG 28 2001
OFFICE OF THE CLERK

(2)

No. 00-1934

IN THE

Supreme Court of the United States

American General Finance, Inc.,
Merit Life Insurance Co., and
Yosemite Insurance Company,

Petitioners,

v.

Mable Branch,

Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of Alabama

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Barry A. Ragsdale
(Counsel of Record)
Garve W. Ivey, Jr.
Ivey & Ragsdale
1615 Financial Ctr.
505 North 20th Street
Birmingham, AL 35203
205/327-5223

Michael J. Quirk
F. Paul Bland, Jr.
Trial Lawyers for Public Justice , P.C.
1717 Massachusetts Avenue, NW, Suite 800
Washington, D.C. 20036
202/797-8600

30 pp

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES ii

INTRODUCTION 1

STATEMENT OF THE CASE 2

A. The Parties' Loan Transaction 2

B. The Loan Transaction in the *Reaves* Case 3

C. American General Finance's Mandatory Arbitration Clause 4

D. The State Trial Court Proceedings 6

E. The Alabama Supreme Court's Holding 9

ARGUMENT 10

I. The Decision of the Court Below is Consistent with *First Options* and Other FAA Cases Addressing Arbitration of "Arbitrability" Disputes 11

II The Holding that Petitioner's Arbitration Clause is Unconscionable is Both Fact-Specific and Consistent with Prevailing Authority on State Contract Law and Federal Preemption 16

CONCLUSION 24

TABLE OF AUTHORITIES

Cases:

Abram Landau Real Estate v. Benova, 123 F.3d 69 (2nd Cir. 1997) 15

Alexander v. Standard Oil, 423 N.E.2d 578 (Ill. 1981) ... 21

Armendariz v. Foundation Health Psychare Services, Inc., 6 P.3d 669 (Cal. 2000) 19

Arnold v. United Companies Lending Corp., 511 S.E.2d 854 (W. Va. 1998) 19

Cole v. Burns Int'l Security Serv's, 105 F.3d 1465 (D.C. Cir. 1997) 20

DeGaetano v. Smith Barney, Inc., 983 F. Supp. 459 (S.D.N.Y. 1997) 20

Derrickson v. Circuit City Stores, Inc., 81 Fair Empl. Prac. Cas. 1553 (D. Md. 1999), *aff'd* 203 F.3d 821 (4th Cir.) (table), *cert. denied*, 530 U.S. 1276 (2000) 20-21

Doctor's Associates, Inc. v. Casarotto, 517 U.S. 681 (1996) 16-17, 23

Doctor's Associates, Inc. v. Hamilton, 150 F.3d 157 (2nd Cir. 1998) 22-23

First Options of Chicago, Inc. v. Kaplan, 514 U.S. 938 (1995) 13-14

Gibson v. Neighborhood Health Clinics, Inc., 121 F.3d 1126 (7th Cir. 1997) 20

Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20 (1991) 17, 23

Hull v. Norton, 750 F.2d 1547 (11th Cir. 1985) 20

Koveleskie v. SBC Capital Markets, Inc., 167 F.3d 361 (7th Cir. 1999) 21-22

Lane v. Garner, 612 So.2d 404 (Ala. 1992) 9, 17

Lloyd v. Service Corp. of Ala., 453 So.2d 735 (Ala. 1984) 17-18

Lozada v. Dale Baker Oldsmobile, Inc., 91 F. Supp.2d 1087 (W.D. Mich. 2000) 20

Matterhorn, Inc. v. NCR Corp., 763 F.2d 866 (7th Cir. 1985) 13

Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614 (1985) 17

Painewebber, Inc. v. Elahi, 87 F.3d 589 (1st Cir. 1996) .. 15

Paladino v. Avnet Computer Technologies, Inc., 134 F.3d 1054 (11th Cir. 1998) 20

Perez v. Globe Airport Security Services, 253 F.3d 1280 (11th Cir. 2001) 20

Perry v. Thomas, 482 U.S. 483 (1987) 23

Prevot v. Phillips Petroleum Co., 133 F. Supp.2d 937 (S.D. Tex. 2001) 14

Prima Paint Corp. v. Flood & Conklin Mfg Co., 388 U.S. 395 (1967) 1, 12-14

Showmethemoney Check Cashers, Inc. v. Williams, 27 S.W.3d 361 (Ark. 2000) 19-20

Taylor v. Leedy & Co., 412 So.2d 763 (Ala. 1982) 18

United Food and Commercial Workers Union v. Lucky Stores, Inc., 806 F.2d 1385 (9th Cir. 1986) 15

Washington-Baltimore Newspaper Guild, Local 35 v. Washington Post, 959 F.2d 288 (D.C. Cir. 1992) 14-15

We Care Hair Development, Inc. v. Engen, 180 F.3d 838 (7th Cir. 1999) 22

Statutes and Regulations:

Alabama Uniform Commercial Code, AL St. 7-2-302 ..... 7, 16, 17, 23

Federal Arbitration Act, 9 U.S.C. §§ 1 *et seq.* ..... *passim*

9 U.S.C. § 2 ..... *passim*

9 U.S.C. § 3 ..... 1, 12

9 U.S.C. § 4 ..... 1, 11

Labor-Management Relations Act, 29 U.S.C. § 185 14

INTRODUCTION

The opinion of the Alabama Supreme Court in this case and the questions presented in the Petition for Certiorari do not warrant a grant of this Court's discretionary review. The holding of the court below was highly fact-specific, based on particular terms of the contractual arbitration provision at issue and on a detailed evidentiary record as to contract formation between these two parties. Indeed, the court below held that the same mandatory arbitration clause was fully enforceable based on different facts relating to contract formation in the companion case of *American General Finance, Inc. v. Reaves*. *See* Pet. 28a-29a. The narrow scope of the holding below thus belies Petitioner's contention that this case is worthy of review because the court below exhibited a "general anti-arbitration bias." Pet. 3. It did nothing of the sort.

Nor does the opinion below conflict with authority from this or other courts on the questions presented. The Alabama Supreme Court held consistent with Sections 2 through 4 of the Federal Arbitration Act and this Court's decision in *Prima Paint Corp. v. Flood & Conklin Mfg Co.*, 388 U.S. 395 (1967), that a court must decide whether an asserted arbitration clause is a valid and enforceable contract before a party can be ordered into arbitration pursuant to it. Likewise, the court's holding that Petitioner's mandatory arbitration clause is unconscionable under the general standards of Alabama's Uniform Commercial Code as they apply to the facts of this case is consistent with decisions of courts across the country. Petitioner fails to identify any contrary authority holding either that a court may order arbitration under the FAA without determining whether the asserted arbitration agreement is unconscionable, or that the FAA preempts generally applicable rules of state contract law.

For these reasons, the Court should not grant review on either of the questions presented in the Petition for Certiorari.

STATEMENT OF THE CASE

Both the trial court and the Alabama Supreme Court below relied on extensive evidence pertaining to the one-sided formation and terms of the mandatory arbitration provision in Petitioner American General Finance's sub-prime loan contract with Respondent Mable Branch to hold that it is unconscionable and cannot be enforced in this case. The fact that the Alabama Supreme Court upheld the very same arbitration clause in the companion case demonstrates that the holding here is limited by the *combination* of the particularly one-sided terms of this arbitration provision and the detailed evidence of American General's control over formation of this contract with Ms. Branch. The holding of the court below is also consistent with decisions of this Court and courts across the country regarding who decides whether an asserted arbitration agreement is unconscionable as a matter of state contract law and regarding the propriety of a party's use of its overwhelming bargaining power to impose a one-sided dispute resolution system that unilaterally limits another party's legal remedies.

A. The Parties' Loan Transaction.

Over the year and a half period from July 1996 to November 1997, Respondent Mable Branch took out a series of three short-term, high interest loans from Petitioner American General Finance, Inc. Ms. Branch borrowed money from American General in July 1996, October 1996, and November 1997. Pet. 2a. She was described by the trial court below as the kind of borrower to whom banks would not be expected to provide loans. *Id.* at 46a.

Through its loans to Ms. Branch, American General Finance is alleged to have collected excessive finance charges and unnecessary or excessive premiums for credit disability and life insurance. *Id.* at 5a. American General also is alleged to have sold duplicative services to Ms. Branch by "flipping" her loans whereby she was induced to refinance existing loans at additional costs. *Id.*

As a condition for obtaining its sub-prime loans, American General required Ms. Branch to give up her right to sue in court and instead submit any future claims she might have against the lender to binding arbitration. American General drafted all of the documentation for these loan transactions. Ms. Branch had no input into the content of these documents and had no meaningful choice regarding the arbitration requirement in seeking a loan through American General Finance. *Id.* at 25a-26a. At the time of Ms. Branch's loans between July 1996 and November 1997, either 14 or 15 out of the 16 finance companies listed in the Tuscaloosa region where Ms. Branch lived required that borrowers waive their right of access to court and submit any future legal claims they might have to binding arbitration as a condition for obtaining a loan. *Id.* at 26a.

B. The Loan Transaction in the *Reaves* Case.

April Reaves also took out a series of short-term, high-interest loans from American General Finance. Ms. Reaves alleged that she too had to pay high finance charges and unnecessary or excessive insurance premiums on her loans, and that she was faced with American General's sale of duplicative services through the practice of flipping loans. *Id.* at 5a.

Ms. Reaves obtained her loans from American General in December 1994 and again in November 1995, before Ms. Branch ever obtained any of her loans. *Id.* at 2a. During this period when Ms. Reaves was borrowing, most finance companies listed in the geographic area where she lived did not require borrowers to submit to arbitration as a condition for receiving their loans. *Id.* at 28a. By borrowing from American General, Ms. Reaves submitted to the company's binding requirement of binding arbitration of all her future legal claims.

C. American General Finance's Mandatory Arbitration Clause.

The mandatory and binding arbitration requirement in American General's finance papers with Ms. Branch initially appears to apply to all claims by either party. The arbitration provision begins: "Borrower and lender agree that, except as otherwise set forth herein in this provision, all claims, disputes, or controversies of every kind and nature between Borrower(s) and Lender shall be resolved by arbitration." *Id.* at 2a. But several paragraphs later, near the end of the arbitration clause, American General reserves only for itself the right to sue in court for virtually any claim it could have against Ms. Branch:

> Borrower(s) and Lender agree that, notwithstanding the foregoing, Lender retains the right to use judicial or self-help remedies (i) to repossess or foreclose on collateral or to enforce the security interests relating to this transaction, and (ii) to pursue collection actions against the Borrower(s) where the amount of the debt is $10,000 or less.

Id. at 4a. Based on the size of Ms. Branch's loans, this saves from the arbitration requirement every foreseeable claim that American General could ever bring against Ms. Branch.

American General's protection of its own right to sue Ms. Branch in court does not extend to any counterclaims raised by Ms. Branch in such suits. Instead, American General retains sole control over the forum for such counterclaims by reserving the right to compel arbitration separate and apart from the litigation of American General's claims against Ms. Branch:

> The exercise of this right by Lender to pursue judicial or self-help remedies shall not constitute a waiver of Lender's right to compel the arbitration of any claim or dispute subject to this arbitration clause—including the filing of a counterclaim by Borrower(s) in a lawsuit filed by Lender.

Id. American General's arbitration clause with Ms. Branch also provides that "**all issues and disputes as to the arbitrability of claims must also be resolved by the arbitrator.**" *Id.* at 3a (emphasis in original).

In addition to the unilateral waiver of Ms. Branch's right to sue in court, American General's arbitration clause imposes limits on the legal remedies that are available to Ms. Branch in arbitration. The arbitration clause limits the amount of punitive damages for which American General may be held liable to Ms. Branch in arbitration without regard to the degree of culpability of its conduct:

> BORROWER(S) AND LENDER AGREE THAT THE ARBITRATOR MAY AWARD PUNITIVE DAMAGES ONLY UNDER CIRCUMSTANCES WHERE A COURT OF COMPETENT JURISDICTION COULD AWARD SUCH DAMAGES. HOWEVER, IN NO EVENT SHALL AN AWARD OF FIVE (5) TIMES THE ECONOMIC LOSS SUFFERED BY THE PARTY.

Id. at 3a-4a. This arbitration provision also imposes a unilateral prohibition on Ms. Branch's participation in any class action proceedings involving the lender: "BORROWER(S) AND LENDER FURTHER AGREE THAT THE ARBITRATOR SHALL NOT CONDUCT ANY CLASS-WIDE PROCEEDINGS AND WILL BE RESTRICTED TO RESOLVING THE INDIVIDUAL DISPUTES BETWEEN THE PARTIES." *Id.* at 4a.

Finally, American General's arbitration clause requires that any arbitration between American General and Ms. Branch shall be conducted according to the commercial rules of the American Arbitration Association. *Id.* at 3a. It further specifies that "[e]ach party shall pay one-half of the arbitration costs and expenses" of such commercial proceedings. *Id.*

D. The State Trial Court Proceedings.

Mabel Branch sued American General Finance, Merit Life Insurance Company, and Yosemite Insurance Company in June 1998 in the Hale County, Alabama Circuit Court alleging that American General's predatory lending practices described above violated Alabama statutory and common law. April

Reaves filed suit against these defendants in September 1998, making substantially the same allegations. *Id.* at 5a.

Petitioners moved the trial court to compel arbitration of both actions based on the mandatory arbitration provision in American General's loan documents. *Id.* The trial court consolidated the two cases for purposes of resolving the arbitration issue. *Id.* at 40a. Ms. Branch and Ms. Reaves argued in response to Petitioners' motions to compel arbitration that the arbitration clause was unconscionable and therefore unenforceable against them as a matter of general Alabama contract law. After allowing discovery on the arbitration issues, the trial court issued its decision on these motions based on an extensive evidentiary record. *Id.* at 40a.

The court first determined that it must apply general state contract law to decide whether or not the parties had agreed to arbitrate before it could address any assertion as to the scope of American General's arbitration clause. *Id.* at 41a. The court then applied Section 2-302 of Alabama's Uniform Commercial Code, which states the general rule that:

> If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause...

AL St. 7-2-302. Pursuant to Alabama Supreme Court precedent on contractual unconscionability outside the arbitration context, the trial court considered whether there was unequal bargaining power and an absence of meaningful choice by one party in the

making of the asserted agreement to arbitrate, and whether the terms of American General's arbitration clause were patently unfair and unreasonably favorable to itself as the controlling party. Pet. 42a.

In addressing these factors, the trial court held that American General's arbitration clause was unconscionable as it would apply in both cases because neither borrower had any meaningful choice as to arbitration and because its terms unreasonably favored American General. Pet. 46a-48a. In support of its finding that Ms. Branch and Ms. Reaves had no meaningful choice, the trial court cited to a number of facts specific to these cases, including admissions by American General that it made arbitration a mandatory condition for its loans; stipulations by other area sub-prime lenders that they too required arbitration during the period in question; and testimony that the borrowers would not have been able to obtain loans from a bank. Pet. 46a. In finding the terms of the arbitration clause to be substantively unfair and unreasonably favorable to American General, the trial court cited to the lack of mutuality in the clause in allowing the lender to sue on nearly all of its possible claims, the unilateral cap on punitive damages that borrowers may recover, and the prohibition on class actions by borrowers. *Id.* at 47a-48a. The trial court also emphasized that American General's stipulation purporting to waive certain contractual prohibitions was further evidence both that the terms of the arbitration clause were unreasonable and that it was an adhesive contract subject to American General's complete control. *Id.* at 47a.

E. The Alabama Supreme Court's Holding

The Alabama Supreme Court affirmed the trial court's judgment in part by holding that American General's arbitration clause is unconscionable only as it applies to Ms. Branch. The court first affirmed that the unconscionability of the arbitration clause is a threshold issue for the court to decide before the parties can be ordered to arbitrate, and that the provision for arbitration of arbitrability disputes takes effect only after a court determines that the arbitration clause itself is enforceable. *Id.* at 20a-21a. The court then held that the trial court correctly applied the indicia of unconscionability under general Alabama contract law, reiterating the factors it had identified nearly ten years earlier in a case not involving arbitration:

> (1) whether there was an absence of meaningful choice on one party's part, (2) whether the contractual terms are unreasonably favorable to one party, (3) whether there was unequal bargaining power among the parties, and (4) whether there were oppressive, one-sided or patently unfair terms in the contract.

Id. at 21a (quoting *Layne v. Garner*, 612 So.2d 404, 408 (Ala. 1992)).

With regard to consumer choice and bargaining power in the formation of this particular arbitration provision, the court found that Ms. Branch had no meaningful choice as to arbitration because American General had insisted on it as a condition of the loans, as did all but one or at most two area lenders at the time of these loans. Pet. 27a. The court found that Ms. Branch had no meaningful choice as to arbitration because she would have had to expend considerable time and

effort to find any alternative. *Id.* at 27a. With regard to the substantive terms of American General's arbitration clause, the court focused on the clause's non-mutual nature in preserving American General's right of access to court for every foreseeable claim it might have against Ms. Branch; the scope of the unilateral arbitration provision in applying to every conceivable claim of Ms. Branch (including claims regarding arbitrability); and the punitive damages cap which would also apply unilaterally to Ms. Branch's claims in arbitration but not to American General's claims in court. *Id.* at 22a-24a. The court emphasized that the *combination* of these provisions, plus the absence of meaningful choice by Ms. Branch, rendered the arbitration clause unconscionable in this case. *Id.* at 24a-25a.

In the same opinion, the Alabama Supreme Court held that American General's arbitration clause should be enforced against April Reaves because she had failed to demonstrate an absence of meaningful choice on her part as to arbitration. The court found that lenders requiring arbitration were a minority where Ms. Reaves was living at the time she secured all of her loans and therefore that she could have found an arbitration-free loan without considerable cost or effort. *Id.* at 28a. The court thus enforced American General's mandatory arbitration provision in her case despite its sweeping and one-sided terms.

ARGUMENT

There is no reason for this Court to review the narrow and fact-specific holding of the Alabama Supreme Court in this case. The court below focused on and limited its holding to the detailed evidence regarding formation of this contract between Petitioner and Respondent. Furthermore, the opinion of the court below is consistent with this Court's decisions and those

of appellate courts from around the country on both of the questions presented. Petitioner has not identified a single case where a court ordered a party into arbitration under the Federal Arbitration Act, 9 U.S.C. §§ 1 *et seq.*, for the threshold determination of whether the asserted arbitration clause that would be the only basis for such an order is unconscionable and therefore unenforceable. Furthermore, Petitioner has produced no authority for its contention that the FAA preempts a State court's application of established and generally applicable principles of unconscionability under the State's Uniform Commercial Code to a contractual arbitration provision. The Court therefore should not take up either of the questions presented in the Petition for Certiorari.

I. The Decision of the Court Below is Consistent with *First Options* and Other FAA Cases Addressing Arbitration of "Arbitrability" Disputes.

The Alabama Supreme Court's holding that a court must resolve attacks on the validity of an arbitration clause, including its provision for arbitration of arbitrability disputes, before the court may order a party into arbitration is a routine application of the Federal Arbitration Act's express provisions and this Court's interpretations of the Act. Section 2 of the FAA states that contractual arbitration clauses are enforceable "save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. Likewise, Section 4 empowers courts to compel arbitration of particular disputes only "upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue." 9 U.S.C. § 4.

Based on these requirements of the FAA, this Court has drawn a sharp distinction between issues related to the validity of an arbitration agreement, which a court must decide before it can order arbitration of a dispute, and other issues relating to contracts with arbitration provisions, which may be reserved for the arbitrator if the arbitration clause itself is enforceable. In *Prima Paint Corp. v. Flood & Conklin Mfg Co.*, 388 U.S. 395 (1967), the Court held that a claim of fraud in the inducement of a contract containing an arbitration clause is subject to arbitration, but that a claim of fraud in the inducement of an arbitration clause is for a court to decide under the FAA. *Id.* at 403-04.[1] The Court explained in *Prima Paint*:

> This position is consistent...with the [FAA's] statutory scheme. As the "saving clause" in § 2 indicates, the purpose of Congress in 1925 was to make arbitration agreements as enforceable as other contracts, but not more so. To immunize an arbitration agreement from judicial challenge on the ground of fraud in the inducement would be to elevate it over other forms of contract —a situation inconsistent with the "saving clause."

---

[1] Although Section 4 of the FAA applies to independent actions to compel arbitration, *Prima Paint* held that the same rules apply to motions under Section 3 to stay litigation on a claim and compel arbitration because it would be "inconceivable that Congress intended the rule to differ depending upon which party to the arbitration agreement first invokes the assistance of a federal court." *Id.* at 404.

Id. at 404 n.12.[2] The lower court's decision in this case regarding who decides under the FAA whether a contractual arbitration clause is valid and enforceable adheres to *Prima Paint*, and Petitioner has identified no authority to the contrary.

Petitioner's attempt to establish a conflict between the holding in this case and *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995), fails because the two decisions address significantly different issues. In *First Options*, it was undisputed that there was a valid arbitration agreement between a stock trade clearing firm and a wholly owned investment company. *Id.* at 940-41. The parties' disagreement was about whether the *scope* of the arbitration clause was broad enough to cover a claim by the clearing firm to recover the company's debts from its owners, and whether a court or an arbitrator should decide this dispute over the scope of the arbitration agreement. *Id.* In answering the second question, this Court held that a court should ordinarily decide whether a particular dispute is covered by an arbitration clause, but recognized that parties may by "clear and unmistakable language" allow an arbitrator to make such an arbitrability determination. *Id.* at 944-45. Since the dispute in *First Options* involved the scope of a presumptively valid arbitration clause, the Court there had no reason to revisit the issue decided in *Prima Paint* and raised in the instant case of whether a party may be ordered into arbitration *before* there is a determination that the asserted arbitration agreement (which would be the only basis for such an order) is a valid and enforceable contract.

---

[2] *See also Matterhorn, Inc. v. NCR Corp.*, 763 F.2d 866, 867 (7th Cir. 1985) ("although section 4...speaks only of challenges to 'the making' of the agreement to arbitrate, the term has been held to encompass any challenge to the validity of the agreement, even if there is no disagreement that it was 'made.'")

The decision below is thus consistent with *Prima Paint* and *First Options* in holding that a court must decide whether an arbitration clause, even one that provides for arbitration of arbitrability disputes, is a valid and enforceable contract before it may order arbitration of any dispute. *First Options* nowhere purports to overturn or modify *Prima Paint*. Indeed, *First Options* never even discusses *Prima Paint* or the FAA's provisions that apply to disputes over the making and enforceability of contractual arbitration clauses like that in the instant case. Since Respondent's unconscionability argument goes to the making and original validity of the asserted arbitration clause, it was properly resolved by the court under the FAA's provisions that this Court applied in *Prima Paint*.[3]

Having failed to demonstrate any conflict between *First Options* and the decision of the Alabama Supreme Court below, Petitioner identifies no other decision that would create a split of authority on its first question presented. In *Washington-Baltimore Newspaper Guild, Local 35 v. Washington Post*, 959 F.2d 288 (D.C. Cir. 1992), the court ordered arbitration of the parties' dispute over whether the arbitration clause in their collective bargaining agreement applied to certain of the employer's pay-scale decisions. This was a dispute over the scope, not the making and validity, of the arbitration clause. Furthermore, this labor relations dispute was governed by Section 301 of the Labor-Management Relations Act, 29 U.S.C. § 185, and thus gave the court no occasion to examine the

---

[3] *See also Prevot v. Phillips Petroleum Co.*, 133 F. Supp. 2d 937, 939 (S.D. Tex. 2001) (case where injured workers did not speak English at time of alleged arbitration "agreement," holding that unconscionability argument against enforcement of arbitration clause is for court to decide under *Prima Paint* even where clause provides for arbitration of arbitrability disputes).

Federal Arbitration Act's provisions regarding the making of agreements to arbitrate. Likewise, in *United Food and Commercial Workers Union v. Lucky Stores, Inc.*, 806 F.2d 1385 (9th Cir. 1986), the court ordered arbitration over whether a union's grievance complied with the specificity requirements of a collective bargaining agreement's arbitration clause. This case too involved an interpretation of an arbitration agreement, not a determination as to its underlying validity, and did not involve the sections of the FAA that apply to this case.[4]

In sum, the court below held that a party cannot be forced into arbitration under the Federal Arbitration Act until a court has first determined that an asserted arbitration agreement, including one that provides for arbitration of arbitrability disputes, is a valid and enforceable contract under generally applicable state law. Petitioner has identified no case holding to the contrary and therefore has established no basis for this Court to grant review on the first question presented.

---

[4] Petitioner cites several cases in a footnote, *see* Pet. at 11-12 n.4, which state generally that disputes over the validity and enforceability of arbitration clauses involve issues of "arbitrability." But none of these cases conflict with the decision of the court below by holding under the FAA that parties must go to arbitration to find out whether or not they entered into a valid and enforceable arbitration agreement in the first place. *See, e.g.*, *Abram Landau Real Estate v. Benova*, 123 F.3d 69, 72 (2nd Cir. 1997) (labor relations case holding that question of on-going application of arbitration clause was arbitrable because it required interpretation of other bargaining agreement provisions, while noting parties' agreement over original validity and applicability of arbitration clause); *Painewebber, Inc. v. Elahi*, 87 F.3d 589, 599 (1st Cir. 1996) (holding that question of whether investors' fraud claims were time-barred by NASD arbitration rules is presumptively for arbitrator to decide and is *not* a question of arbitrability).

II. The Holding that Petitioner's Arbitration Clause is Unconscionable is Both Fact-Specificand Consistent with Prevailing Authority on State Contract Law and Federal Preemption.

Petitioner confuses the highly fact-specific holding of the Alabama Supreme Court regarding the enforcement of its contractual arbitration provision in this case for a generalized attack on all arbitration agreements in all cases. The court below applied Section 2-302 of the State's Uniform Commercial Code to hold that Petitioner's arbitration clause is unconscionable based on the combination of its particularly one-sided terms and the detailed evidence showing that Respondent had no meaningful choice as to arbitration in the making of this loan contract. The limitation of this decision to this combination of facts is demonstrated by the court's holding in the companion case that the same one-sided arbitration clause was enforceable against another borrower who was shown to have greater choice as to arbitration at the time of her loans. Pet. 28a-29a. The decision below is neither a broad-based attack on arbitration in general nor even an attack on all applications of this particularly one-sided arbitration provision. Instead, it is a narrow application of general rules of Alabama contract law to the specific facts presented in this case.

The Alabama Supreme Court's decision below is consistent with the command of the Federal Arbitration Act and this Court's opinions interpreting the Act to subject contractual arbitration provisions to the same rules of state law that apply to other contracts. In *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681 (1996), the Court explained that Section 2 of the FAA places arbitration agreements on the same footing with other contracts so that "generally applicable contract defenses

such as fraud, duress, or unconscionability, may be applied to invalidate arbitration agreements without contravening § 2." *Id.* at 687. Likewise, in *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991), the Court noted Section 2's savings provision and warned that "'courts should remain attuned to well-supported claims that the agreement resulted from the sort of fraud or overwhelming economic power that would provides grounds for the revocation of any contract.'" *Id.* at 33 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 627 (1985) (internal quotation omitted)). The court below did just this, applying previously recognized and generally applicable indicia of unconscionability under the Alabama U.C.C. and finding these indicia to have been established through a detailed evidentiary record.

The Alabama Supreme Court held that Petitioner's arbitration clause is unconscionable in this case under indicia of unconscionability that the court had recognized nearly ten years earlier in a case that did not involve arbitration. Pet. 21a (citing *Layne v. Gardner*, 612 So.2d 404, 408 (Ala. 1992). The court based its finding that Respondent had no meaningful choice as to arbitration and was subject to Petitioner's overwhelming bargaining power on an evidentiary record which demonstrated that nearly every area lender required arbitration during the time period in question and that Petitioner had made arbitration a mandatory condition for its loans. Pet. 26a-28a. Petitioner mistakenly asserts that the court below had never ruled outside the context of arbitration that market prevalence is relevant to the issue of consumer choice as an indicium of unconscionability, Pet. 19. In *Lloyd v. Service Corp. of Ala.*, 453 So.2d 735 (Ala. 1984), the Alabama Supreme Court did precisely this regarding the use of exculpatory clauses in landlord-tenant contracts, finding that:

> 'The tenant has no meaningful choices. He can accept this landlord or go to another landlord who charges the same rent and asks the tenant to sign the same standard form lease. In other words, the modern standard form lease is in essence an adhesion contract. A survey of residential leases in Alabama would show that almost all contain these exculpatory clauses.'
>
> ...That consumer, in need of goods or services, is frequently not in a position to shop around for better terms, because all competitors use the same clauses.

Id. at 739 (quoting *Taylor v. Leedy & Co.*, 412 So.2d 763, 766 (Ala. 1982) (Faulkner, J., concurring specially).[5] The court's finding of procedural unconscionability in contract formation is thus both fact-specific to this case and well-supported under established principles of general Alabama contract law.

---

[5] Petitioner also mistakenly suggests that the court below ignored its previous cases by finding unconscionability even though Ms. Branch is an educated and sophisticated consumer. Pet. 16. This argument is flatly contrary to the facts in the record: Ms. Branch is a self-employed beautician in a rural community who took two years of cosmetology classes at a local vocational school. Prior to working as a beautician, she was employed as a laborer constructing wooden pallets. She testified in the case that she did not understand the loan documents in the case, and specifically did not understand the language of the arbitration clause. For example, Ms. Branch testified that she does not understand the meaning of the word "litigate." In light of this detailed record which conflicts with Petitioner's characterization of the facts, there is no occasion for this Court to second-guess the integrity of the Alabama Supreme Court's analysis of how Alabama contract law applies to these facts.

Even in the absence of meaningful choice as that term is defined under Alabama contract law, Petitioner's arbitration clause would likely have been enforced in this case had it not also diminished Respondent's substantive legal rights by imposing a unilateral cap on her recovery of damages. The Alabama Supreme Court nowhere said that market prevalence of a contractual term *by itself* renders the term unconscionable. Instead, the court invoked widely recognized standards of substantive unconscionability in holding that the terms of Petitioner's particular arbitration clause are one-sided and unreasonably favorable to American General.

The court emphasized the scope of the arbitration clause as it would require arbitration of all of Respondent's claims (including those relating to arbitrability), while carving out from this requirement every foreseeable claim that Petitioner might ever have, and the fact that Respondent alone would be subject to unilateral remedial limitations in arbitration. Pet. 22a-24a. A sizable body of case law from courts around the country has similarly treated such non-mutuality as an indicium of unconscionability.[6] Numerous courts have also recognized

---

[6] *See, e.g., Armendariz v. Foundation Health Psychare Services, Inc.*, 6 P.3d 669, 692-94 (Cal. 2000) (arbitration clause in employment contract is unconscionable where it applies only to employee's claims and places unilateral limits on employee's damages: "The unconscionable one-sidedness of the arbitration agreement is compounded in this case by the fact that it does not permit the full recovery of damages for employees, while placing no such restriction on the employer."); *Arnold v. United Companies Lending Corp.*, 511 S.E.2d 854, 861-62 (W.Va. 1998) (holding arbitration provision in lender's contract with elderly couple unconscionable where lender "like rabbit and foxes" affected a "wholesale waiver of the Arnolds' rights together with the complete preservation of United Lending's rights.") (quotation omitted) *Showmethemoney Check Cashers, Inc. v. Williams*, 27 S.W.3d 361, 365-66 (Ark. 2000) (payday lender's arbitration

that arbitration provisions which limit a party's access to legal remedies that are available in court may be unenforceable.[7]

---

clause is unenforceable under Arkansas contract law for lack of mutuality where lender's collection claims are exempted but all of the borrower's claims are covered); *Gibson v. Neighborhood Health Clinics, Inc.*, 121 F.3d 1126, 1131 (7th Cir. 1997) (arbitration clause in employment contract is unenforceable under Indiana law for want of consideration where clause applies to employee's claims but exempts employer's claims); *Hull v. Norton*, 750 F.2d 1547, 1550-51 (11th Cir. 1985) (arbitration provision in employment contract is unenforceable under New York law for want of consideration where employer reserves own right to sue in court; court finds no preemption because case falls within Section 2 savings clause).

[7] *See, e.g., Cole v. Burns Int'l Security Serv's*, 105 F.3d 1465, 1482 (D.C. Cir. 1997) (arbitration must offer "all the types of relief that would otherwise be available in court"); *Paladino v. Avnet Computer Technologies, Inc.*, 134 F.3d 1054, 1062 (11th Cir. 1998) (Cox, J., concurring for majority of court) (arbitrability of Title VII claims "rests on the assumption that the arbitration clause permits relief equivalent to court remedies. . . . When an arbitration clause has provisions that defeat the remedial purpose of the statute . . . the arbitration clause is not enforceable."); *Perez v. Globe Airport Security Services*, 253 F.3d 1280, 1286-87 (11th Cir. 2001) (holding arbitration clause that prevents prevailing Title VII plaintiff from recovering attorney's fees to be unenforceable); *DeGaetano v. Smith Barney, Inc.*, 983 F. Supp. 459, 469 (S.D.N.Y. 1997) (voiding arbitration clause disallowing attorneys' fees for prevailing Title VII plaintiff, concluding that "contractual clauses purporting to mandate arbitration of statutory claims . . . are enforceable only to the extent that the arbitration preserves the substantive protections and remedies afforded by the statute."); *Lozada v. Dale Baker Oldsmobile, Inc.*, 91 F. Supp.2d 1087, 1105 (W.D. Mich. 2000) (finding as to consumer Truth In Lending Act and state consumer protection act claims that "both federal and Michigan case law support a conclusion that an arbitration provision is substantively unconscionable because it waives class remedies, as well as declaratory and injunctive relief"); *Derrickson v. Circuit City Stores, Inc.*, 81 Fair Empl. Prac. Cas. 1533 (D. Md. 1999) (arbitration clause capping punitive damages and back pay remedies under Section 1981 is unenforceable), *aff'd*, 203

These cases hold not that all or most arbitration clauses are unconscionable, but only that particular types of arbitration provisions similar to those found here may be unconscionable in certain cases. The holding of the court below is thus consistent with case law recognizing the need for courts to enforce general principles of state contract law in unusually one-sided and unfair circumstances in order to prevent businesses from abusing their bargaining power by turning private arbitration proceedings into an occasion to diminish unilaterally the substantive legal rights of individual consumers.

Petitioner has identified no authority that conflicts with the Alabama Supreme Court's decision or supports the extraordinary contention that preemption under the FAA extends to prohibit enforcement of established standards of unconscionability under a State's Uniform Commercial Code. In *Koveleskie v. SBC Capital Markets, Inc.*, 167 F.3d 361 (7th Cir. 1999), the court held that an arbitration provision in an employment contract was not unconscionable as a matter of Illinois contract law whether or not it was adhesive because there had been no attempt to show that its terms were substantively unfair. *Id.* at 367 ("'the disparity in the size of the parties entering into the agreement...without some wrongful use of that power,' is not enough to render an arbitration agreement unenforceable.'") (quoting *Alexander v. Standard Oil*, 423 N.E.2d 578, 580 (Ill. 1981)). These requirements are entirely consistent with the unconscionability standards applied by the Alabama Supreme Court based on the very different contract in this case. Both decisions closely examine disparities in bargaining power during contract formation and substantive unfairness in the terms of the arbitration clause. What's more,

---

F.3d 821 (4th Cir.) (table), *cert. denied*, 530 U.S. 1276 (2000).

since *Koveleskie* turned on interpretations of Illinois contract law, any perceived difference with the decision below would not give rise to a question of federal law in any event.[8] Finally, while *Koveleskie* stated in dicta that a hypothetical state rule prohibiting enforcement of all pre-dispute arbitration agreements would be preempted by the FAA, *supra* at 367, this in no way conflicts with the instant case because the court below never intimated such a rule and in fact *enforced* a pre-dispute arbitration clause in the companion case.

Likewise, Petitioner's discussion of the Second Circuit's opinion in *Doctor's Associates, Inc. v. Hamilton*, 150 F.3d 157 (2nd Cir. 1998), establishes no conflict with the decision of the court below here. First, the court in *Hamilton* rejected the defendant's unconscionability argument not because it was preempted but because the party had waived the argument by failing to raise it in the trial court. *Id.* at 164. *Hamilton* did hold that a state statute prohibiting forum selection clauses in franchise contracts was preempted to the extent that it would operate to prohibit enforcement of an arbitration provision in such a contract. *Id.* at 163. But the court found that there was preemption under Section 2 of the FAA because this statutory rule was not generally applicable; rather it "applies to one sort of contract provision (forum selection) in only one type of

---

[8] For the same reason, Petitioner's reliance on *We Care Hair Development, Inc. v. Engen*, 180 F.3d 838 (7th Cir. 1999), invokes no question of federal law. The Seventh Circuit there again applied Illinois contract law to find that a franchise agreement's arbitration provision was not unconscionable based solely on its non-mutual nature. *Id.* at 843. It is also noteworthy that the court in *We Care* emphasized the relative equality in bargaining power between parties to a franchise contract, noting that "the franchisees were not vulnerable consumers or helpless workers, but rather business people who bought a franchise." *Id.* (internal quotation omitted).

contract (a franchise agreement)." *Id.* The rule of unconscionability invoked by the Alabama Supreme Court in this case, by contrast, applies to all contracts under the State's U.C.C. and has been recognized generally by this Court in *Gilmer* and *Casarotto* not to be preempted based on the savings clause in Section 2 of the FAA. *Hamilton* therefore does not in any way conflict with the holding in the instant case.[9]

The Federal Arbitration Act's goal of enforcing voluntary agreements to arbitrate is perfectly consistent with the Alabama Uniform Commercial Code's concern for ensuring meaningful choice and substantive fairness in the formation of contracts. Neither policy goal is satisfied where a borrower is forced to submit to arbitration in order to obtain any loan and where a lender abuses this advantage in bargaining power by imposing a one-sided arbitration requirement that unilaterally restricts the borrower's available legal remedies. The holding of the court below was narrowly based on a detailed factual record on each of these points and does not conflict with decisions of this or other courts on the scope of FAA preemption. This case therefore does not warrant this Court's discretionary review on either of the questions presented.

---

[9] The argument herein that *Hamilton* does not conflict with the holding of the court below is in no way a concession that *Hamilton* was correctly decided under this Court's FAA preemption rulings. The anti-forum selection clause statute in *Hamilton* neither "takes its meaning precisely from the fact that a contract to arbitrate is at issue," *Perry v. Thomas*, 482 U.S. 483, 492 n. 9 (1987), nor creates "threshold limitations placed specifically and solely on arbitration provisions," *Casarotto*, 517 U.S. at 688. Still, that question is not presented in the instant case because the unconscionability ruling of the court below is neither limited to specific types of contracts nor to specific types of contractual clauses.

CONCLUSION

The petition for a writ of *certiorari* should be denied.

Respectfully submitted,

Barry A. Ragsdale
(Counsel of Record)
Garve W. Ivey, Jr.
Ivey & Ragsdale
1615 Financial Center
505 North 20th Street
Birmingham, AL 35203
205/327-5223

Michael J. Quirk
F. Paul Bland, Jr.
Trial Lawyers for Public Justice , P.C.
1717 Massachusetts Ave., NW, Suite 800
Washington, D.C. 20036
202/797-8600

Counsel for Respondent

Date: August 28, 2001